In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 139

WALTER F. TELLIER AND EVELYN H. TELLIER,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

The issue presented by this petition [1] is essentially one of fact—whether securities sold by petitioner [2]

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[1] The petition is addressed to the first of two issues litigated below. The second issue was resolved in favor of the petitioner by the court of appeals and the Commissioner's time to file a petition for a writ of certiorari has been extended to June 16, 1965.

[2] Petitioner's wife is a party only because she and her husband filed joint returns.

were held primarily for sale to customers in the ordinary course of petitioner's business, thus making the gains on sale ordinary income rather than capital gain. The Tax Court found for the goyernment and the Court of Appeals for the Second Circuit affirmed (Pet. 29-32, R. 4a-30a).[2]

From 1945 to 1956, first as an individual and later as controlling (90%) partner in Tellier and Company, petitioner was in the business of underwriting securities sold to the public for less than $1 per share and purchasing securities for resale to customers. Pursuant to the underwriting agreements, Tellier and Company "nominated" petitioner to receive stock or stock warrants from the companies whose stock was being underwritten. Petitioner frequently sold these warrants or shares of stock through Tellier and Company (Pet. 31; R. 5a-9a). There were seventy separate transactions of this kind during the years 1952-1956 (the taxable years here in question) from which petitioner's annual profits varied between $13,000 and $97,000 (Pet. 31-32; R. 10a-19a). On some occasions, as an inducement to make more sales of the publicly issued shares, taxpayer gave Tellier and Company's salesmen part of his stock warrants. Tellier and Company at all times had free call upon the securities which taxpayer kept in what was designated by him as an "investment account." The cashier of Tellier and Company had authority to borrow any security it might need either because of a

[2] "R" references are to the appendix to the petitioner's brief in the court of appeals.

short sale or because a security had not been received (Pet. 32; R. 9a-10a).

Section 1221(1) of the Internal Revenue Code of 1954 (like its identical predecessor) excludes from classification as capital assets any "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." The capital gains tax is designed to give preferential tax treatment to profits arising from investments, as distinguished from the profits of everyday business operations. *Corn Products Co.* v. *Commissioner*, 350 U.S. 46, 52. In order to effectuate this purpose "the definition of a capital asset must be narrowly applied and its exclusions interpreted broadly." *Ibid.* The Tax Court sustained the Commissioner's determination that the gains from the securities sold by the taxpayer were taxable as ordinary income, rather than as capital gains, on the ground that (Pet. 32):

> The volume of sales, petitioner's activities with respect to the securities, and the close relationship between petitioner's investment accounts and the dealing activities of Tellier and Company support the conclusion that the securities here involved were being held by petitioners for sale to customers in the ordinary course of their trade or business.

The court of appeals affirmed, stating that "There is ample evidence to support the Tax Court's finding that the taxpayer held the securities for sale in the ordinary course of business" (Pet. 31).[4]

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[4] Neither court found it necessary to reach the government's alternative argument that petitioner's profits were in the

Petitioner does not challenge these findings of fact. Instead he argues that as a matter of law Section 1236 of the 1954 Code compels capital gain treatment for any stocks that a securities dealer has labelled an investment (Pet. 18-21). The argument is without merit. As is plain from its language and history, Section 1236 (like its identical predecessor) was intended to narrow, not to broaden the category of securities gains that would qualify for capital gain treatment. It expressly applies only if (1) the security was *not* held primarily for sale to customers, and (2) the security was clearly identified in the dealer's records as held for investment. The section is inapplicable if *either* of these two requirements is not met. As the Senate Finance Committee Supplemental Report stated:

> the mere fact that a security, which is actually held by the dealer for sale to customers in the ordinary course of the trade or business, is identified as required by this section as a security held for investment, will not cause the gain from the sale of the security to be treated as capital gain. [S. Rep. No. 781, Part 2, 82d Cong., 1st Sess., p. 47 (1951-2 Cum. Bull, 545, 577).]

Since both courts below found that the securities involved in the instant case were held primarily for sale to customers in the ordinary course of petitioner's

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nature of compensation for personal services. Cf. Treas. Regs. §§ 1.61-15, 1.421-6.

business, petitioner derives no benefit from Section 1236.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ARCHIBALD COX,
Solicitor General.

LOUIS F. OBERDORFER,
Assistant Attorney General.

HARRY BAUM,
ROBERT A. BERNSTEIN,
Attorneys.

JUNE 1965.

END